§ 549(a)
Mistake
§ 363(c)(1)

Plaid Pantries, Inc. v. Core-Mark Distrib., Inc., Adversary No. 89-3214 S
In re Plaid Pantries, Inc., Case No. 389-30128 S11

11/30/1990 L. Tchaikovsky Unpub.

The debtor sought to recover postpetition payments made by the debtor in possession to a vendor for the purchase of goods supplied to debtor's affiliate. The debtor contended that the disputed payments could be recovered under § 549(a) and as a mistaken payment under Oregon law. The court rejected the debtor's arguments and denied recovery.

With regard to § 549(a), the court held that the payments were authorized by § 363(c)(1), which allows a trustee or debtor in possession operating a debtor's business to enter into transactions and use estate property in the ordinary course of business, without notice or a hearing.

The court also concluded that the debtor was not entitled to recover the payments under Oregon law as mistaken payments. The court found that although the debtor made the payments by mistake, they were not recoverable because Oregon law does not permit recovery when the payee has changed its position in reliance on the mistaken payment.

P90-44(13)

U.S. BANKRUPTCY COURT
DISTRICT OF OREGON
FILED

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UNITED STATES BANKRUPTCY COURT

FOR THE DISTRICT OF OREGON

In re

PLAID PANTRIES, INC., an Oregon corporation,

Debtor.

CASE NO. 389-30128 S11

PLAID PANTRIES, INC., an Oregon corporation,

Plaintiff,

vs.

CORE-MARK DISTRIBUTORS, INC., a Nevada corporation,

Defendant.

ADVERSARY PROCEEDING NO. 89-3214 S

MEMORANDUM OF DECISION

This adversary proceeding concerns the attempt by a debtor-in-possession to recover, on various legal theories, approximately $99,000 in post-petition payments made by the debtor-in-possession to a vendor for the purchases of the debtor's affiliate. For the reasons stated below, the Court finds for the defendant.

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SUMMARY OF FACTS

Plaintiff Plaid Pantries, Inc. ("Plaid") filed a voluntary petition seeking relief under chapter 11 of the Bankruptcy Code on March 14, 1990. Plaid is the principally owned subsidiary of Pacific Crest Equities, Inc. ("Pacific Crest"). Both before and after the filing of the bankruptcy petition, Plaid operated over a hundred convenience stores in several states.

Pacific Crest has other subsidiaries, including Franko Oil ("Franko"). Franko is not a debtor in a bankruptcy case. Franko operates gas stations, some of which also sell snack food and other products similar to those sold in the convenience stores operated by Plaid.

Defendant Core-Mark Distributors, Inc. ("Core-Mark") sells snack foods and other products to convenience stores and other similar retail outlets. For some time prior to Plaid's bankruptcy filing, Core-Mark sold products to both Plaid and Franko.

It is undisputed that, before Plaid's bankruptcy filing, there was little care taken by Plaid or Franko to keep corporate operations separate. The two corporations occupied the same office space and had employees who performed services for one corporation who were carried on the payroll of the other corporation. Bills for one corporation were paid by the other if the other happened to have money available when the bill was received and the one who had received the product did not.

Corporate distinctions were not totally disregarded.

Appropriate debits and credits were made on the books of the two corporations to reflect payments made or other services provided by one corporation to or for the benefit of the other. At the time of Plaid's bankruptcy filing, Franko owed Plaid approximately $1 million on account of such payments made or services provided by Plaid to or on behalf of Franko.

When Plaid's bankruptcy was filed, both Plaid's way of doing business and its course of dealing with Core-Mark and its other vendors changed dramatically. Like most of Plaid's vendors, Core-Mark insisted on payment on a C.O.D. basis. Pacific Crest, on the other hand, brought in an individual named John Wiencken ("Wiencken") as what it called a "crisis manager" to improve operations. Wiencken tried to establish a clear division between the operations of Plaid and Franko. Initially, the operations of the two corporations were physically separated within the same office space. Later, Franko moved its operations to a separate office space. Employees were instructed that funds of one company were not to be used for purposes related to the other company. For the most part, employees served only one or the other of the two corporations. However, even after Wiencken's arrival, there was apparently some overlap in employees between the two corporations.

Prior to Plaid's bankruptcy filing, Plaid and Franko purchased products from Core-Mark on normal credit terms. A copy of the invoice was delivered to the store purchasing the product with the product. The store manager would send it to the corporate office which would pay the invoice in due course. When Plaid was put on a C.O.D. basis by its vendors, it asked its vendors to provide its corporate office with a copy of the invoice for the product for which payment was to be made on the day payment was required. Core-Mark was unable or unwilling to do so. Instead, Core-Mark agreed to either mail a copy of the invoice or make it available to be picked up a day after the payment was made. The total amount of the payment for product delivered to all stores was called into the corporate office.

The Plaid employee responsible for the C.O.D. payments testified that, whenever these figures were called in by Core-Mark, she always asked whether these figures were solely for Plaid deliveries and was assured that they were. She testified that she did so because Wiencken had impressed upon her the importance of keeping the operations of Franko and Plaid separate. Notwithstanding these assurances, the figures called in and paid by Plaid during the six weeks following the bankruptcy filing were later discovered to have included $99,574.47 in charges for product delivered to Franko (the "Disputed Payments").

Another Plaid employee testified that she had had several conversations with Core-Mark employees complaining about the inclusion of Franko charges. This employee claimed she had sent the Core-Mark accounts payable person copies of stores lists on two occasions during the first six weeks of Plaid's bankruptcy. She also testified that she believed a list had been provided to

Core-Mark prior to the bankruptcy filing. At the end of the six weeks, apparently because of Plaid's inability to agree upon mutually satisfactory course of dealing, Plaid ceased purchasing product from Core-Mark.

Core-Mark's accounts receivable person testified that she had never been informed, prior to the termination of Plaid's business relationship with Core-Mark, that Plaid and Franko were separate corporations. She had been told by her supervisor that they were separate divisions of Pacific Crest. She pointed to a business card which had been provided to her by Plaid's accounts payable person which listed Pacific Crest, not Plaid. Plaid employees admitted that there had been some discussion of changing Plaid's name to Pacific Crest-AM/PM. Certain forms used by Core-Mark had been changed at the instruction of employees of Plaid to designate the company in this manner whereas formerly they had differentiated between Plaid and Franko. The Core-Mark accounts receivable person also denied that she had ever seen a store list until just prior to the termination of Plaid's business relationship with Core-Mark.

SUMMARY OF ARGUMENT

Plaid contends that the Disputed Payments may be recovered under 11 U.S.C. §549(a) as unauthorized post-petition payments. Furthermore, it contends that the Disputed Payments may be recovered under Oregon law as payments made by mistake. Core-Mark contends that, while not authorized by the Court, the Disputed Payments were authorized by the Bankruptcy Code. While

Core-Mark appears to concede that Plaid made the Disputed Payments by mistake, Core-Mark notes that, under Oregon law, a mistaken payment may not be recovered if the payee has detrimentally relied on its receipt. Core-Mark contends that it detrimentally relied on the receipt of the Disputed Payments by providing the goods in question to Franko.

A. AVOIDANCE OF PAYMENTS UNDER 11 U.S.C. §549

Section 549(a) of the Bankruptcy Code provides, in pertinent part, that:

> ...the trustee may avoid a transfer of property of the estate -
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> ...
>
> ...that is not authorized under this title [title 11] or by the court.

The Disputed Payments were not authorized by the court. However, they were authorized by title 11: i.e., the Bankruptcy Code. Section 363(c)(1) provides that if the business of the debtor is to be operated, unless the Court orders otherwise, the trustee or debtor-in-possession "...may enter into transactions...and may use property of the estate in the ordinary course of business without notice or a hearing." Ninth Circuit case law establishes a two pronged test for determining whether certain financial transactions are in the ordinary course of business. In re Dant & Russell, Inc., 853 F.2d 700, 704-05 (9th Cir. 1988). The first prong is referred to as the horizontal test: i.e., whether other businesses of this type would engage in the subject

2transaction in the normal course. Id. at 704. The second prong is referred to as the vertical test: i.e., whether it was customary for this debtor prior to filing its bankruptcy to enter into transactions of this sort in the normal course. Id. at 705.

The definition of the transaction determines the outcome of the decision. If the transaction is viewed broadly--the purchase of goods for resale--no sensible argument that either test is not met. A retail business could not operate without the routine purchase of goods for resale. Core-Mark anticipated that the transaction would be defined narrowly: e.g., as payments made for the goods of an affiliate. It attempted to prove at trial that it is was customary or at least not unusual for one corporation to pay expenses of an affiliated corporation. It is undisputed that this was Plaid's customary practice prior to the filing of its bankruptcy petition.[1]

The Court is not fully persuaded that the Disputed Payments would meet the horizontal test of Dant & Russell, supra if the payment by Plaid for sales to Franko had been intentional. However, the Court was persuaded that the Disputed Payments were made inadvertently. Under these circumstances, the Court believes that the transaction should be defined more broadly, as

[1]The Court notes and rejects Plaid's argument that the debtor's pre-petition course of dealing cannot be considered in determining whether a transaction was in the ordinary course of business because the debtor-in-possession is a distinct legal entity from the debtor. The business is the same, even if the entity operating it is not.

the purchase of goods for resale. Thus, the Disputed Payments are not avoidable under Section 549(a).

An argument might be made, although Plaid has not made it, that the Disputed Payments were not in the ordinary course of business because made on a C.O.D. basis. Presumably, most businesses of this type do not purchase goods for resale on a cash basis. Clearly, Plaid did not do so prior to filing its bankruptcy case. Since the argument was not raised, the Court need not decide it. However, the Court would be reluctant to order the payments recovered on this basis because of the devastating effect it would have on a debtor's ability to persuade vendors to continue selling to it after a bankruptcy petition is filed.

The cases cited by Plaid--In re St. Mary's Hospital, 101 B.R. 451 (Bankr.E.D.Pa. 1989), In re Lockwood Enterprises, Inc., 54 B.R. 829 (Bankr.S.D.N.Y. 1985), and Braniff Airways, Inc. v. Exxon Company USA, 814 F.2d 1030 (5th Cir. 1987)--are totally inapposite. None of the three relies on Section 549(a). Because the Court finds for defendant on this ground, it need not address the availability of equitable defenses to actions to avoid transfers under the Bankruptcy Code.

B. RECOVERY OF PAYMENTS UNDER OREGON LAW

Plaid notes that, under Oregon law, a party may recover a payment made by mistake. Gonyea v. Rich, 283 Or. 261, 583 P.2d 539 (1978); Smith v. Rubel, 140 Or. 422, 13 P.2d 1078 (1932). It further notes that the payment may recovered even if the mistake was solely the fault of the payor and was not in any respect induced by the payee. Snow v. Tompkins, 205 Or. 60, 286 P.2d 119 (1955); Adams v. Crater Well Drilling, Inc., 276 Or. 789, 556 P.2d 679 (1976).[2] Core-Mark does not attempt to dispute this rule of law. Instead, it attempts to distinguish the cases cited by Plaid and bring itself within the exceptions to this rule.

Core-Mark notes that, in Gonyea v. Rich, supra, the Court found for the defendant. In that case, the plaintiff advanced money to the defendant in the expectation that the plaintiff would be made a partner is a limited partnership to be formed in the future. The payments apparently advanced the anticipated enterprise of the limited partnerships. The Court found that the plaintiff knew of the uncertainties of the transaction when he advanced the money and concluded that it would be unfair to require the defendant to repay the money. Similarly, in Adams v. Crater Well Drilling, Inc., supra, the Court acknowledged the general rule that, where a bill known to be disputed is paid, it cannot later be recovered as a payment by mistake. In that case, however, the Court found that the defendant's conduct was so egregious that recovery was warranted.

Core-Mark argues that this general rule should be applied in the instant case, that Plaid knew or should have known that the

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[2]In Davis v. Tyee Industries, 295 Or. 467, 479, 668 P.2d 1186 (1982), the Court held that Snow was disapproved to the extent that it was inconsistent with Davis' holding that ultimate facts establishing a right to recovery of punitive damages must be specifically alleged. Id.

Disputed Payments were for Franko's purchases. They knew best which stores belonged to Franko and which to Plaid. They could have devised a way to determine the amount of purchases by each store on a given day if they had wanted to do so. Thus, the Disputed Payments should not be deemed mistaken.

The Court is not persuaded by Core-Mark's argument. The knowledge of the plaintiffs in Gonyea, supra, and Crater Well Drilling, supra, was actual not imputed. Core-Mark is simply arguing that Plaid was negligent in making the Disputed Payments. However, as noted by Plaid, under Oregon law, a mistaken payment may be recovered even if the mistake was negligently made. Smith v. Rubel, 140 Or. 422, 426-427, 13 P.2d 1078, 1078 (1932).

Smith v. Rubel, supra, 140 Or. at 426-427, 13 P.2d at 1079 limits the application of the rule permitting recovery of mistaken payments by excluding payments which have caused the payee to change its position such that it would be unjust to require the payment to be returned. Core-Mark argues that this limitation should preclude recovery of the Disputed Payments from it. This Court agrees. Core-Mark contends that it changed its position by entering into a stipulated judgment with Franko for a lesser amount than the full amount of its debt. Had it known of the Disputed Payments, it would have insisted on a stipulated judgment in a higher amount. The Court was not persuaded by the evidence presented that Core-Mark was prejudiced by the Disputed Payments in this respect. The evidence suggested that the Core-Mark had notice of at least some of the Disputed Payments prior to entering into the stipulation. Moreover, the value of a stipulated judgment against Franko in any amount appeared questionable based on the evidence presented to the Court.

Core-Mark has not forcefully argued the change in circumstances which appears the most apparent to the Court, perhaps because it is too obvious. Core-Mark agreed to sell to Plaid after the bankruptcy petition was filed only if it were paid in cash at the time of delivery. Clearly, it wished to take no risk in connection with future sales to Plaid. Core-Mark changed its circumstances as result of its receipt of the Disputed Payments by delivering the goods.

However, the limitation on the recovery of mistaken payments noted in Smith v. Rubel, supra, requires not just a change in circumstances, but one made in reliance on the mistaken payment. This requires the Court to make a factual determination as to Core-Mark's state of mind in requesting the Disputed Payments. If the Court believed that Core-Mark acted fraudulently--that its personnel intentionally represented to Plaid that payments were due for deliveries to Plaid that they knew had been delivered to Franko, it would find in favor of Plaid. Under those circumstances, it could not be said that Core-Mark changed its circumstances in reliance on the Disputed Payments since it could not fairly rely on its right to retain payments obtained through fraud.

However, the Court does not believe that Core-Mark's personnel acted fraudulently. This determination rests

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principally on the testimony of one witness--Charlene Gothard, Core-Mark's Assistant Credit Manager. Ms. Gothard testified that she did not know that Plaid and Franko were separate corporations, that she had never had store lists until the end of the period during which the Disputed Payments were made, and that she does not recall being asked whether the figures quoted included Franko bills. The Court did not believe that she was lying.

Moreover, the equities tip in favor of Core-Mark. The problem arose because of the way in which Plaid and Franko had done business prior to the filing of Plaid's bankruptcy petition. Core-Mark may have been somewhat uncooperative in the early post-petition weeks in helping Plaid change that way of doing business. However, Core-Mark was forthright as to what it was and was not willing to do. When Plaid agreed to pay for deliveries based on a telephone call, without verifying invoices or checking with its own store managers as to the deliveries received, given its past course of dealing, Plaid took the risk that some of the payments might mistakenly go for product delivered to Franko. Even after Wiencken had impressed Plaid and Franko with the importance of keeping the two companies' affairs separate, there was some overlap. As one witness observed: "Old habits die hard."

CONCLUSION

Plaid may not recover the Disputed Payments pursuant to Section 549(a) of the Bankruptcy Code. The payments were made in the ordinary course of business and thus were authorized by Section 363(c) of the Bankruptcy Code. In addition, Plaid may not recover the Disputed Payments under Oregon law as payments made by mistake. Although the Court was convinced that the payments were made by mistake, Oregon law does not permit recovery when the payee has changed its position in reliance on the mistaken payments. Core-Mark changed its position in reliance on the Disputed Payments by delivering product to the stores in question. The Court did not believe that Core-Mark fraudulently represented to Plaid that Disputed Payments were due for deliveries to Plaid stores, knowing that they were in fact due for deliveries to Franko stores. Plaid took the risk that mistakes would be made when it agreed to pay Core-Mark cash for purchases without being provided with an invoice. Absent fraud, it would be unfair to shift that risk to Core-Mark after the fact. Core-Mark is directed to prepare and submit a form of judgment in accordance with this memorandum.

Dated: November 19, 1990

Leslie Tchaikovsky
United States Bankruptcy Judge

cc: Jeffrey Misley
Christopher Blattner

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U.S. BANKRUPTCY COURT
DISTRICT OF OREGON
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IN THE UNITED STATES BANKRUPTCY COURT

FOR THE DISTRICT OF OREGON

PLAID PANTRIES, INC., an Oregon corporation, Plaintiff, v. COREMARK DISTRIBUTORS, INC., a Nevada corporation, Defendant.	Case No. 389-31028-S11 Adversary Proceeding No. 89-3214-S JUDGMENT

This action came on for hearing before the Court, Honorable Leslie Tchaikovski, Bankruptcy Court Judge, presiding, and the issues having been duly heard and a decision having been duly rendered,

IT IS HEREBY ORDERED AND ADJUDGED that the plaintiff take nothing, that the action be dismissed on the merits, and that the defendant, Coremark Distributors, Inc., recover of the plaintiff, Plaid Pantries, Inc., its costs of this action.

DATED this 17th day of December, 1990.

Leslie Tchaikovsky
~~Clerk of the Court~~

Presented by:

BLATTNER & RUNIA

Christopher C.S. Blattner
OSB #82194
of Attorneys for Defendant Coremark

cc: Sylvia E. Stevens
Christopher C. S. Blattner

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CERTIFICATE OF MAILING

I hereby certify that I served the foregoing

JUDGMENT

on the following attorney on December 7, 1990, by mailing to said attorney a true copy thereof, certified by me as such, contained in a sealed envelope, with postage paid, addressed to said attorney at said attorney last known address, to-wit:

Sylvia Stevens
SUSSMAN, SHANK, ET AL.
1001 S.W. 5th Avenue, Suite 1111
Portland, Oregon 97204

and deposited in the post office at Portland, Oregon, on said day.

DATED this 7th day of December, 1990.

BLATTNER & RUNIA

Christopher C.S. Blattner
OSB# 82194
of Attorneys for Coremark